

MARKET AND ECONOMIC UPDATE

June Quarter 2025

KEY POINTS

- **Equity Markets Saw Considerable Gains:** Equity markets were highly volatile, with sharp declines following aggressive US tariff announcements, but later rebounding strongly. Global equity markets recorded significant gains led by the US, and the Australian market also climbed an impressive 9.5%.
- **Trump 2.0 Effect:** Trump once again moved markets with his tariff-policy announcements. A sharp sell-off in markets followed before he announced a 90-day pause, which eased investors' nerves. His involvement in the Israel–Iran conflict also generated concern as it heightened the risk of global escalation. Lastly, the latest bill to be approved will add a tremendous amount of debt to the US, which caused volatility in the bond market.
- **Bond Prices Were Volatile:** Bonds ended the quarter up, although yields were bashed around by announcements from the White House. Shorter-duration bonds are focusing on central-bank rate cuts, whilst longer-duration bonds are concerned with aggressive fiscal policy.
- **US Dollar Weakness:** The US dollar continued to weaken in Q2 2025 due to concerns about the US economy. Reduced economic prospects made the US less attractive compared with economies with higher growth potential. The risk of higher US debt provided further downward pressure on the dollar.

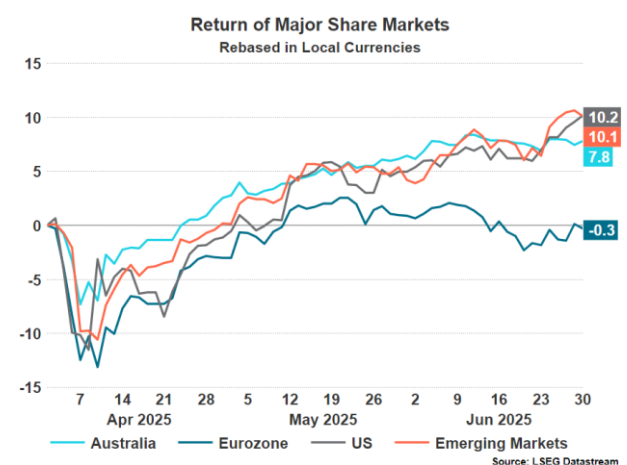
1. MARKETS IN REVIEW

Over the last three months, Donald Trump unveiled an onslaught of aggressive tariff policies, causing a significant global sell-off. He subsequently announced a reconsideration of these controversial measures in an attempt to calm the market.

A conflict between Israel and Iran also spooked markets and narrowly avoided triggering a third world war. It is therefore surprising that equity markets have taken this in their stride and continued to trend upwards, with some indices reaching all-time highs. The S&P 500 returned 10.94%, whilst the tech-heavy NASDAQ delivered an impressive 16.73%. The Australian market was not exempt from the rally, rising by 7.78%.

Fixed income experienced similar volatility, as bond investors assessed to what extent these tariff measures would feed into inflation and economic-growth forecasts, ultimately impacting rate-cut expectations. The Australian and global fixed-income markets followed suit, seeing a gradual fall in bond yields.

In April, the uncertainty generated by Trump's tariff announcements provided a tailwind for defensive assets. Gold climbed above the US \$3,400 mark for the first time in history, before a slight correction as investors locked in profits. Oil prices also rose on the back of the Middle East conflict, before moderating once a ceasefire was agreed.



2. EQUITIES

Equities experienced significant volatility over the quarter. On ‘Liberation Day’, Donald Trump unveiled his much-anticipated tariff policies, which were far more aggressive than markets had priced in. His proposal to stimulate the domestic economy was not well received, and investors feared the measures would trigger re-inflation and push the economy into recession. As a result, risk assets sold off aggressively: the S&P 500 fell 4.88%, whilst expensive growth stocks bore the brunt of the fallout, with the NASDAQ plunging 5.97%—its largest single-day decline in history. The Australian market also declined, albeit to a lesser extent than its global counterparts.

Following the extreme market reaction, President Trump announced a 90-day pause to allow negotiations to proceed. This immediately eased investors’ nerves, triggering a surge in investment as market participants sought to ‘buy the dip’. Over the subsequent week, the S&P 500 rallied by approximately 7%, whilst the tech-heavy Nasdaq gained around 9%. The Australian market mirrored these global trends, though to a lesser extent given limited direct trade exposure with the US.

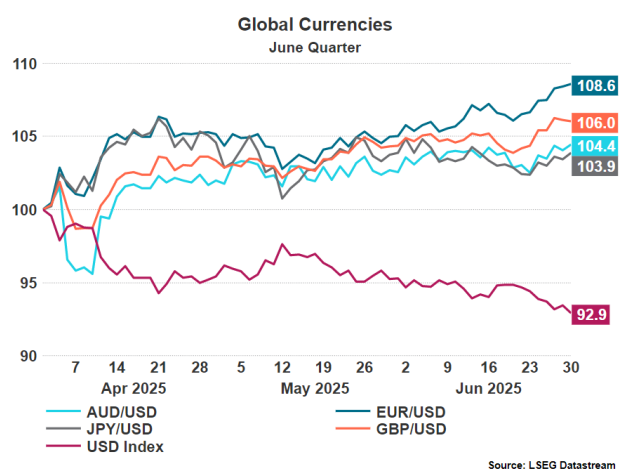
A conflict between Iran and Israel also sparked uncertainty as the threat of global escalation loomed. However, the hostilities lasted only 12 days before a ceasefire was agreed, and there was no sustained impact on equity markets over the quarter.

Overall, almost all equity markets ended the quarter in positive territory, largely due to the prevailing belief that President Trump would now need to adopt a more measured approach to tariffs. Risk assets outperformed defensive assets, signalling a return to the new normal where technology giants lead the charge. While the tariff threats posed little risk to Australian exports, the potential economic impact on Australia’s largest trading partner, China, was certainly taken into account.

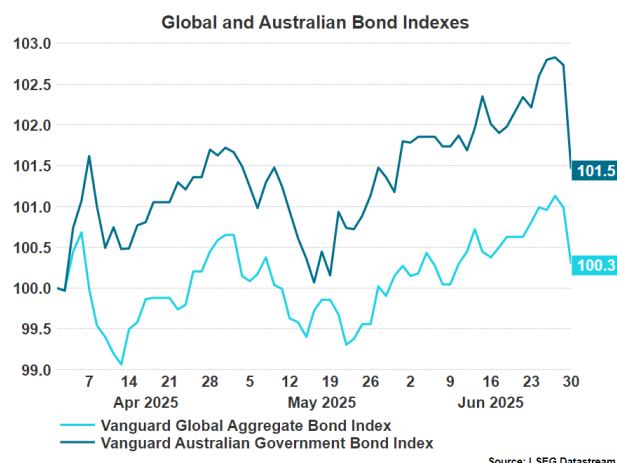
3. FOREIGN EXCHANGE MARKETS

Over the second quarter of 2025, the US dollar slid sharply, with the US Dollar Index falling by almost 7%—its worst start to a year since 1995. Markets were unsettled by the prospect that a fresh wave of tariffs would dampen growth, by fears of soaring US debt under the so-called “Big Beautiful Bill”, and by growing scepticism over the dollar’s long-standing role as a safe-haven asset. Having traded at elevated levels for an extended period, the currency was ripe for a correction back towards more typical valuations.

As the dollar weakened, its major peers all gained ground. The Australian dollar, Japanese yen, euro and pound sterling appreciated noticeably, driven predominantly by the dollar’s decline. In addition, stronger economic performance in the eurozone and the Reserve Bank of Australia’s cautious approach to monetary easing provided further tailwinds for both the euro and the AUD.



4. FIXED INCOME MARKETS



Fixed income markets also experienced a volatile quarter as investors sought to price in how the tariff policies would affect inflation and recession risk. As illustrated in the chart, global bond yields (which move inversely to bond prices) initially fell following 'Liberation Day', only to rise once the 90-day pause was announced. They then drifted lower through April as investors judged an economic slowdown to pose a greater threat than inflation, prompting markets to price in additional rate cuts from central banks.

In May, attention shifted from tariffs to the 'Big Beautiful Bill', which could add between \$3 trillion and \$5 trillion of debt to the US economy over the next decade. That prospect steepened the yield curve, widening the gap between short-term and long-term yields: short-duration yields fell on growing rate-cut expectations, while long-duration yields rose amid forecasts of increased issuance of long-dated US Treasuries to fund the debt.

Australian bonds moved in step with US Treasuries, with investors now awaiting the RBA's early-July rate decision, while European bonds outperformed after the European Central Bank (ECB) delivered two rate cuts in response to cooling inflation.

5. OUTLOOK

Looking ahead to the second half of 2025, market volatility is likely to persist as investors digest unfolding economic developments. They will watch final tariff announcements, assess the probability of the "Big Beautiful Bill" passing Congress and parse incoming economic releases for clues about the timing of rate cuts. President Trump's erratic policymaking is expected to remain a key market mover—his decision to impose, then pause, tariffs in response to a global sell-off demonstrates just how influential he can be. As such, investors should guard against sudden swings by maintaining a globally diversified portfolio.

Domestically, Australia's outlook appears more encouraging. Easing inflation should give the Reserve Bank of Australia scope to begin cutting interest rates, especially as business-condition indicators continue to improve. Given the sensitivity of Australian households to mortgage-rate movements, any RBA rate reduction is likely to provide a meaningful boost to the economy.

Fixed Income:

Fixed income markets are expected to remain volatile as analysts pore over data on future growth and inflation, which will ultimately influence central-bank interest-rate decisions. Because these macroeconomic indicators are notoriously difficult to forecast accurately, a diversified fixed-income approach is advisable. Investors should remember that, despite the risks, bond yields at current levels are highly attractive offering not only diversification from growth assets but also compelling income. In such an uncertain landscape, appointing a manager who can capitalise on spikes in yields while capturing front-end income is likely to deliver stronger long-term performance.

Credit markets both public and private remain appealing, though ongoing slowdown risks and potential re-inflation call for a selective focus on high-quality issuers. In the US, investors await the fate of the 'Big Beautiful Bill', which could increase federal debt by an estimated US\$ 3.9 trillion over the

next decade, driving up long-term yields as the Treasury issues more long-dated notes. Although two rate cuts are pencilled in for the remainder of the year, bond yields will be chiefly driven by the economic data that inform the Federal Reserve's decisions. In Australia, the Reserve Bank is also likely to begin cutting rates in the second half of 2025 provided no significant shocks derail its traditionally cautious stance.

Equities:

Although AI is likely to continue driving earnings, valuations remain a concern, with large-cap US growth companies trading well above their long-term averages. Now that these firms constitute a substantial portion of major indices, any price correction is likely to weigh on broader markets. Investing in capitalisation-weighted indices such as the S&P 500 exposes investors to significant AI and tech-stock risk, so it's important to be mindful of this sector bias when considering passive exposure. Looking ahead, a rotation into value stocks may prove profitable as growth valuations remain stretched.

The outlook for Australian equities is positive, underpinned by anticipated RBA rate cuts and an improving domestic economic backdrop, although pockets of elevated valuations—particularly in the banking sector—remain a concern. European equities also look attractive, supported by recent ECB rate reductions and substantial fiscal spending, though geopolitical risks continue to loom. Further US-dollar weakness should provide a tailwind for emerging-market equities. China, despite its own set of challenges in recent years, remains interesting on a valuation basis, although the shape of any US–China tariff agreement is as yet unclear; in addition, an ageing population poses a long-term demographic headwind.

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